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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

7 1997

OFFICE OF SECRETARY

In the Matter of	)	
	)	**IB Docket No. 96-261**
International Settlement Rates	)	
	)	

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COMMENTS OF HONGKONG TELECOM INTERNATIONAL

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SUMMARY

Hongkong Telecom International ("HKTI") supports the Commission's objectives for reform of the accounting rate system to more accurately reflect cost conditions and to operate more effectively in modern telecommunications markets. However, HKTI submits that the specific actions proposed by the Commission will exacerbate rather than solve international settlements problems. The unilateral prescription and enforcement by the United States of lower accounting rates between the U.S. and other countries, without concomitant adjustments to U.S. carrier pricing practices, will further distort international traffic patterns. It also will have no foreseeable salutary impact on the development of international competition and no demonstrated direct benefits for U.S. consumers.

HKTI describes in detail that the international settlements process is multifaceted and complex. Problems arising in this process are due to traffic imbalances. Traffic imbalances have many causes, including demographics of users as well as customer arbitrage of collection rates offered in a particular country and carrier arbitrage of accounting rates through such measures as refile, transiting and reverse call options.

It is the growth of reverse call services, such as country direct and call back, which has so aggravated the U.S. settlements deficit in recent years. The Commission essentially ignores this factor. HKTI submits that a proper calculation of any U.S. "deficit" must omit traffic associated with these services, as U.S. carriers earn handsome profits on them. Also, there is every reason to believe that U.S. consumers are subsidizing, not settlement outpayments which are exceeded by significant retained earnings, but below cost pricing by U.S. carriers of reverse call services in foreign markets. Moreover, there is ample evidence that U.S. international collection charges have not declined, and in some cases have actually <u>increased</u>, in the wake of accounting rate reductions.

Hong Kong provides an important example. In the early 1980s, traffic between Hong Kong and the U.S. was balanced, and U.S. carriers made no settlement payments to Hong Kong. With the inauguration of call back, country direct, calling card and similar reverse charge services, traffic became very imbalanced. The ratio of incoming (from the U.S.) to outgoing (to the U.S.) traffic in Hong Kong is now approximately 7:1. During the same period of these developments, U.S.-Hong Kong accounting rates declined. Most importantly, HKTI collection rates to the U.S. declined while AT&T's international collection rates increased. It is clear that the Hong Kong-U.S. imbalance of traffic is <u>not</u> due to arbitrage of collection rates in Hong Kong.

Reverse charge services "dumped" into the Hong Kong market by U.S. carriers at prices below settlement rates constitute unfair competition for HKTI. This is especially true because HKTI does not have complete flexibility to respond competitively. Hong Kong's Office of Telecommunications Authority requires payment by HKTI of national delivery fees for all international traffic. These fees reflect Hong Kong social and economic policy. They also constitute a floor for HKTI international rates. Further reductions of Hong Kong-U.S. accounting rates will only permit more aggressive selling by U.S. carriers of below cost reverse charge services in the Hong Kong market, further aggravating the traffic and settlements imbalance.

Aside from the specific difficulties with the Hong Kong market, HKTI believes that the Commission's general logic on the causes and solutions to settlement rate issues is based upon faulty assumptions not supported by actual evidence. There no evidence that any settlements deficit is a direct result of above cost accounting rates. There is also no evidence that unfair burdens are placed on U.S. consumers as a result of any such deficit. It is true that U.S. consumers are paying higher international rates than they should. However, this is completely by the choice of U.S. carriers seeking to maximize profits. Without mandated corresponding reductions in U.S. collection charges, there is no guarantee U.S. consumers will benefit from the Commission's proposed reductions in benchmark accounting rates.

Similarly, the Commission has not demonstrated that its unilaterally prescribed accounting rate reductions will result either in more competition or fairer competition in international markets. There is no evidence that above cost accounting rates dampen demand for IMTS services or that settlement payments provide the predominant rationale for foreign administrations to resist introduction of competition. Moreover, there is no evidence that, by eliminating "monopoly rents," reductions in accounting rates would help prevent anticompetitive behavior of foreign monopoly carriers seeking entry to the U.S. market. To the extent that foreign carriers may desire to cross subsidize anticompetitive behavior in the U.S., they can always do so through profits, regardless of whether accounting rates are reduced. Finally, as demonstrated by U.S. carriers in foreign markets, cross subsidization can fund anticompetitive behavior in the form of below cost reverse charge services, even when there is a settlements "deficit."

It is also not clear that the Commission's proposals would result in more even traffic flows. Rather there is every reason to expect that they would exacerbate traffic imbalances. Lower U.S. accounting rates will increase incentives to flow traffic through the U.S. market, increasing U.S. settlement outpayments.

HKTI believes that in any event the Commission does not have the right under international law, or the jurisdiction under the Communications Act of 1934, as amended, to prescribe benchmark accounting rates that essentially represent termination charges for foreign markets. Additionally, HKTI believes that the Commission's proposals to condition authorizations under Section 214 on achievement of benchmark accounting rates could not be applied in any fair or uniform way, and thus would be arbitrary and capricious.

Finally, it is HKTI's view that the Commission's proposed benchmark costing methodology is inappropriate. Different costing methodologies reflect particular social and economic policies. The policies favored by the U.S. may not necessarily be deemed suitable by foreign administrations. Accounting rates are intended to reflect an equal sharing of costs of termination on both ends of international calls. Thus, "cost based" accounting rates reasonably must reflect a melding of different countries' views on cost allocation. It is wholly inappropriate for any one country to impose its policies and views unilaterally on the multinational accounting rates system, as such asymmetric practices will only increase distortions in the system.

HKTI strongly urges the Commission not to adopt its proposals as outlined, but instead to work in full cooperation with other administrations and within existing multilateral initiatives on accounting rate reform. HKTI stands ready to fully participate in any such appropriately constituted multilateral efforts.

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To: The Commission

COMMENTS OF HONGKONG TELECOM INTERNATIONAL

Hongkong Telecom International ("HKTI"), by its attorneys, submits these comments in the above captioned proceeding on the Commission's proposals to adopt new rules concerning international accounting rate benchmarks. HKTI is an international carrier, authorized by the government of Hong Kong, which interconnects with U.S. international service carriers. As such, its interests may be directly affected by the outcome of this proceeding.

HKTI does not take issue with the Commission's overall objective of promoting accounting rate reform. The accounting rate system, which evolved within a PTT-based industry structure, is increasingly out of step with modern service configurations and multi-carrier markets. HKTI also commends the Commission for its substantial efforts to estimate costs in the absence of actual interconnection data. However, HKTI does take issue with the Commission's specific proposals.

As HKTI describes below, not only are the Commission's proposals not warranted in the case of Hong Kong, but also the general rationale behind them is faulty. HKTI further questions the Commission's jurisdiction to take the proposed actions. Additionally, because international settlements issues are multilateral and multidimensional, approaching them from a unilateral and unidimensional perspective will only cause more distortions than presently exist. HKTI recommends that pursuit of appropriate multilateral solutions addressed to the overall accounting rates system is a better course.

I. INTRODUCTION AND BACKGROUND

The Commission's stated goal in this proceeding is to ensure that U.S. consumers have available to them an array of technologically advanced international services at reasonable rates. The Notice proposes to achieve this goal by moving aggressively to reform accounting rates ostensibly to promote development of competition in the global market for communications services. The Commission rationalizes that reforms are necessary because above cost accounting rates cause distortions in international markets, including economic incentives favoring monopolies, higher than necessary collection rates and international traffic imbalances resulting in a large "deficit" of international settlement outpayments made by U.S. carriers. Among the particular reforms proposed are the prescription by the Commission of new accounting rate benchmarks which, after a transition period, will serve as a ceiling on the level of accounting rates that can be agreed to by U.S. international carriers in their negotiations with foreign correspondents. In setting the benchmarks, the FCC proposes to use a costing methodology derived in the context of U.S. domestic interconnection proceedings, namely the "TSLRIC" (total service long run incremental cost) methodology.

The proposals advanced by the Commission -- and the rationale upon which they are based -- are superficially appealing. A growing U.S. settlements "deficit" may be a compelling reason for action. Concerns for market distortions caused by asymmetries between competitive and monopoly markets are a valid concern. Reduction of apparently above cost accounting rates seems to be a straightforward solution to these problems. However, the Commission's position is only superficially logical. On close examination the issue is much more complex than the Commission's approach indicates, and significant logical gaps in the Commission's analysis are apparent.

Specifically, the apparent evils of a U.S. settlements deficit and foreign monopoly markets have not been, and cannot be, causally linked to above cost accounting rates. More importantly, the Commission has not demonstrated that reduction in accounting rates will produce the promised benefits of more competitive international markets and lower prices to U.S. consumers. Because there is a fundamental disconnect between the problems cited by the Commission and the proposed solutions, HKTI believes the Commission's proposals cannot be sustained. A brief review of salient features of the accounting rates and settlements system may provide a useful foundation for the detailed discussion below.

First, the level of accounting rates does not necessarily directly impact any settlements imbalance. Unlike access charges, accounting and settlement rates are not intended to reflect the specific costs that a particular carrier incurs for termination of international calls, but an equal sharing of approximated costs incurred by both carriers on a given bilateral route. Thus, the "settlement rate" traditionally is half of the accounting rate. Because the rate is equal in both directions, actual payments are made only on imbalanced minutes. In other words, as the Commission acknowledges, on any bilateral route the carrier that originates more minutes than its correspondent within the settlement period makes a settlement payment only on the "net" minutes.[1] If traffic is balanced, no payments are made from one carrier to

[1] Notice at ¶ 6.

another. This is true regardless of the level of accounting rates, and regardless of whether they are "cost based."

Second, because settlement payments are based on "net" minutes, the real direct cause of any settlement imbalance is a traffic imbalance. Thus, one has to look to the underlying causes of traffic imbalances to find the reason for settlement imbalances.

Traffic imbalances are due in part to carrier arbitrage of varying accounting rates around the world. The very structure of the accounting and settlement rate system creates incentives for carriers to minimize settlement costs and seek least cost routing. As an initial matter, it must be recognized that the accounting rate system applies only to international message telephone services ("IMTS"). Settlements are not paid under this system for private line services. Also, carriage of calls between certain countries may be cheaper if they "transit" a third country. Additionally, carriers have begun to use various forms of "refile."[2] These activities -- which would continue regardless of whether particular accounting rates are cost based -- have a worldwide impact on calling patterns and contribute to traffic imbalances between particular countries.[3]

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[2] This technique makes a call from country A transiting through country B and terminating in country C "look," for settlements purposes, like a call from B to C. This permits the originating carrier of country A to avoid paying settlements on the initial "leg" of a call between countries A and B carried on private lines, and to pay only the lower settlement rate between countries B and C.

[3] Because of this, the problem of "private line bypass" cited by the Commission as resulting from above cost accounting rates actually would exist even with cost based accounting rates, and will persist as long as there are different settlement arrangements for IMTS and private line services. The Commission has long experienced a similar problem in domestic services with the "leaky PBX" phenomenon and the difficulties of devising economically based private line access surcharges to discourage economic bypass.

Traffic imbalances also are created in part by customer "arbitrage" of collection rates in a given country. Customers in countries with relatively high international rates either prefer to accept calls originated in the U.S. or utilize less expensive reverse call services such as country direct, call back, international 800 and calling card services. These services, which make cheaper U.S. calling rates available for calls actually originating overseas, may be subsidized by U.S. carriers, which is the case with call back in Hong Kong. There are a myriad of reasons for higher collection rates in foreign countries. The Commission postulates that above cost accounting rates create a floor for foreign collection charges that keep them higher than U.S. charges, fueling consumer preference for access to U.S. dial tone at lower U.S. rates. However, national traffic balances are related to national tariffs and relative levels of international collection charges, which reflect individual country social and economic policies on telecommunications sector development. Critically, there is no evidence that high accounting rates are the primary reason for high international rates or that reductions in accounting rates will result in lower collection charges.

Third, the Commission's characterization of U.S. settlement outpayments as a "deficit" due principally to above cost accounting rates is vastly oversimplified and misleading. A very significant factor in the growth of the deficit is the burgeoning popularity of U.S. carrier initiated reverse call offerings To this extent, the "deficit" is self-inflicted. An accurate calculation of a "U.S. balance of trade" for IMTS should "back out" settlements associated with such services. They actually reflect traffic inbound to the U.S. Any settlements paid in connection with such services are more than covered by the direct revenues and profits earned on them by U.S. carriers. In any event, a much more relevant consideration of the impact of the settlements process on U.S. carriers is their retained earnings. These have been steadily growing, notwithstanding above cost accounting rates.

As international markets evolve, new service configurations and calling charge options involving reverse calling, transiting, refiling and bypass, will create increased incentives for carriers to market directly to customers in foreign markets as well as to actively search for least cost, though sometimes circuitous, routes. As a result, traffic patterns increasingly will be affected on a global scale. It is deceptively facile, and probably incorrect, to conclude that the deficit would be proportionately smaller if only accounting rates were cost based. In fact, because lower accounting rates with U.S. carriers will increase incentives worldwide for carriers to refile and transit traffic through the U.S. on its way to third country destinations, implementation of the Commission's proposals may make the deficit worse, as the U.S. would become even more of a global hub than it is at present.

Finally, and most critically, U.S. settlements outpayments cannot be shown to constitute transfer payments from U.S. consumers to foreign companies. The Commission's premise that such outpayments are essentially monopoly "rents" extracted by foreign monopolies completely ignores the responsibility U.S. carriers themselves bear for increased U.S collection rates as well as settlement payments due to reverse call services. The truth is that U.S. carriers enjoy substantial retained earnings, despite the so-called "deficit." The above cost collection rates paid by U.S. consumers do not enable transfers of profits to foreign carriers, but instead permit U.S. carriers themselves to make significant subsidized profits themselves on below cost reverse charge services offered in foreign markets. There is certainly no evidence that accounting rate reductions will result in lower calling charges for U.S. consumers. Again, evidence is to the contrary.

Consequently, it cannot logically be concluded that reduction in accounting rates with the U.S. will induce foreign administrations and carriers to accelerate transitions to competition. The opposite may be true. A perception that adoption of the Commission's "benchmark" accounting rates would increase incentives for the flow of traffic through the U.S. market may encourage foreign carriers to do what they can to prevent further erosion of their international revenues.

The U.S. is not alone in experiencing settlement imbalances and in desiring reform to the accounting rate system. HKTI also experiences net settlement outpayments with many other countries, and would directly benefit from accounting rate reform. However, to benefit from such a change would require changes not only to the international settlement structure with the U.S. but to the accounting rate between Hong Kong and all correspondent carriers. Additionally, it would require a change to the national delivery fee structure in Hong Kong (and presumably elsewhere), which is integrally connected to the settlement system. In contrast, because this system is worldwide and multilateral in nature, aggressive unilateral action by the U.S. on only one aspect of what is a complex and multifaceted international issue, may have deleterious rather than beneficial results.

II. THE PROPOSED REFORMS ARE NOT JUSTIFIED IN THE CASE OF HONG KONG

A. Traffic Imbalances Causing Outpayments By U.S. Carriers to Hong Kong Are Not Due To Above-Cost Accounting Rates

The conventional measure for traffic balance is a ratio between incoming and outgoing minutes, a ratio of below 1:1 indicating a network is a net generator of traffic and a ratio of over 1:1 indicating that a network is a net receiver. In the early 1980s, the ratio for HKTI was below 1:1, i.e., Hong Kong sent more minutes to the U.S. than in the other direction. This position has changed dramatically in recent years, and has gone through a number of distinct and identifiable phases.

In the late 1980s, AT&T started to heavily promote international use of their calling card. This was done on a bilateral basis, and in many cases AT&T sold their card in other administrations, with the prior agreement of the local carriers concerned. This practice was a market share play by AT&T, and was soon followed by MCI and Sprint. The net effect of this activity was to reverse billing flows. Thus, although calls were initiated from Hong Kong they were billed in the U.S. and traffic balances moved to approximately 1.2:1.

Despite this move, HKTI agreed to reduce the Hong Kong-U.S. accounting rate by 57% in the following five years (1991-96), showing a commitment to the bilateral process of accounting rate reduction despite an increasingly inbound traffic balance.

Shortly after this agreement, U.S. carriers started to develop supply agreements with major U.S. resellers which involved international calls being sold below settlement, i.e., below the accounting rate outpayment. The logic for this was that as traffic balances were not far from balance (1.2:1 in the Hong Kong case), the application of U.S. proportionate return policies would generate an inpayment which would more than recover the losses in outpayment. The increase in market share benefitted U.S. carriers, and MCI, Sprint and others entered this "subselling" market energetically, entering into long term contracts with U.S. resellers. Traffic balances did not change, as the traffic being fought over was U.S. originated.

By 1990, the "subsale" rates were so low (in some instances one half of the <u>settlement</u> rate) that it was economic for a reseller to automatically reverse billing direction, and early versions of call back were born. Calls initiated by customers overseas generated a call from the U.S. By 1995, traffic balance ratios had moved to 2.5:1.

The increase in the imbalance resulted directly from activity in the U.S., made possible because of selling below cost, i.e. the settlement rate, which created a situation where customers in non-U.S. networks were being offered service by U.S. resellers at rates with which the local administration could not compete. The U.S. consumer was unaware of this activity, was not affected by it in any way, and more importantly was not able to gain the benefit from the lower prices offered by the U.S. carriers, as they were strictly confining their below cost prices to customers with extremely large volumes, i.e., the resellers.

As subsale rates fell further, it became possible for the U.S. call back operators to offer "two leg" service, and to offer access from their target markets overseas to destinations beyond the U.S., i.e. refile. Traffic initiated by callers in Hong Kong would be connected through callback to a switch in the U.S., and onward to any other country. Subsale rates were paid by the reseller to the U.S. carrier for both legs of the call. The traffic imbalance soared to over 6:1.

The resellers are successful because the practice of selling below settlement has made it economical for traffic which normally would have been connected directly between the terminal countries to pass through the U.S. Furthermore, the use of call back has resulted in this traffic being set up as two outgoing calls from the U.S., severely distorting traffic balances. U.S. consumers are not involved, do not originate or received any of the traffic concerned, and more importantly do not pay for it.

In the last two years, the U.S. carriers themselves have started to promote two leg refile. AT&T is actively marketing their AT&T USA Direct service outside the U.S., offering access beyond the U.S. to non-U.S. consumers. This includes giving away US$20 stored value calling cards in Asia, traffic resulting from which will distort traffic balances even if AT&T does not gain new customers. AT&T has launched its own call back service in a number of countries, including Hong Kong and Japan. Both of these products will further distort traffic balances and U.S. outpayments, but presumably are to AT&T's benefit or they would not have launched the services.

In addition to two leg refile using call back, the principal U.S. international carriers have been actively seeking refile traffic which directly generates calls both incoming to and outgoing from the U.S. Rates are low, as the U.S. carriers are relying on revenues from proportionate return and other means. In some cases the incoming traffic flow to the U.S. is delivered over dedicated trunks, and may not appear in incoming traffic statements, with the net effect of increasing outgoing traffic from the U.S. even further.

The case of Hong Kong graphically illustrates that much of the problem that the Commission ascribes to above cost accounting rates is in fact a result of the assiduous efforts by U.S. carriers to "game the system" to maximize profits. These efforts are manifested by the "dumping" of below cost priced services in foreign markets, attraction of bulk refile through the U.S. and maintenance of above cost collection charges for U.S. consumers. The case of Hong Kong also indicates that, far from promoting fair competition in international markets, unilateral requirements by the U.S. for further reductions in accounting rates, without other concomitant changes in the accounting rates process, will only result in further transfers of revenue from foreign markets to U.S. carriers. This is plainly not the result the Commission ostensibly seeks.

B. Traffic Imbalances Causing Outpayments By U.S. Carriers to Hong Kong are Not Due To Collection Rate Arbitrage

1. Hong Kong International Calling Rates are Competitively Priced

International calls in Hong Kong are competitively priced, and by and large tend to be priced lower than calls in the reverse direction. For example, the filed standard rate for a three minute call from Hong Kong to the U.S. is HK$20.40 (US$2.61), against a similar call to Hong Kong from the U.S. which costs HK$45.79 (US$5.87) in the standard rate period and HK$27.77 (US$3.56) in the economy period.[4]

The business of offering international services to Hong Kong consumers is intensely competitive and it is possible to obtain discounts from all the local operators. Levels as low as HK$5.49, or US$0.70, for a three minute call to the U.S. exist in the Hong Kong market. It can be seen that the standard collection rates are substantially lower than those experienced by U.S. consumers, and the discounted rates even more so. This clearly indicates that no part of the Hong Kong/U.S. traffic imbalance is due to differentials between collection rates in the two countries as is often alleged.

Also, it is difficult to reconcile the statement in paragraph 5 of the Notice, which claims that the current system "significantly increases prices for U.S. consumers," with actual experience. The accounting rate between Hong Kong and the U.S. has declined by 57% in the last five years. Yet, the consumer rates charged by AT&T for calls to Hong Kong have been increased a number of times in the same period. A further reduction in account rates of 20% already has been agreed to with all U.S. carriers providing service to Hong Kong. It can be clearly seen that from a consumer price perspective, the level of accounting rates does not impede reductions in U.S. collection rates. Quite to the contrary, reductions in accounting rates are not passed through but in fact are met with U.S. rate increases. In stark contrast, collection rates in Hong Kong, together with those in many other countries, have in fact declined progressively in the same period.

The charts attached hereto - derived from data in the FCC's August 1996 report Trends in the International Telecommunications Industry - demonstrate that this is a general

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[4] These U.S. rates were drawn from AT&T's Tariff FCC No. 27 filed November 8, 1996, and are assumed to be current.

pattern.[5] Lower settlement rates for the 34 countries reported by the FCC have not resulted in lower prices to U.S. consumers but rather have contributed to the continually increasing net revenues of U.S. carriers - also demonstrated by FCC data.

2. Hong Kong Delivery Fees Reflect National Objectives

The Hong Kong delivery fee as set by the Office of the Telecommunications Authority (OFTA), reflects a balance between international and local charges. In the case of Hong Kong, OFTA has set this rate at HK$2.23, or US$0.29. The US$0.29 represents a cost of doing business for HKTI in Hong Kong, over and above the cost of providing international circuits and switched capacity.[6]

Most countries have delivery fees, both for internal accounting where there is one carrier for both international and national switching (in either a monopoly or competitive environment) and for inter-company settlements where more than one operator is involved. The establishment of these fees is clearly the sole prerogative of the national government concerned, and such changes will be made with due regard to domestic considerations including national policy on market development and demographics such as average income levels. The Commission's proposal essentially ignores these national considerations.

From a Hong Kong perspective, the tariff balance approved by government has resulted in a low cost for local line rentals, at HK$67 (US$8.60) per month for a residential line, with local calls not being charged as part of the monthly rental - i.e., no local message

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[5] Appendix A includes Charts 1-3 demonstrating relative changes over time in Hong Kong - U.S. collection rates charged by HKTI and AT&T. Appendix B includes several charts, derived directly from data presented in Table 11 of the 1996 International Trends report, comparing percentage changes in collection rates and accounting rates for several countries during the years 1990-96.

[6] The Commission indicates incorrectly that the "national extension price" for Hong Kong is "zero." Notice, Appendix E.

rate. The dominant local telephone network provider, Hongkong Telephone, has a collection rate cap of Retail Price Index minus 4% for line rental charges, and cannot rebalance its tariffs without a change to this policy. Such a change would require approval of the Hong Kong Legislative Council. The FCC's proposed unilateral action is clearly in conflict with the Hong Kong government's policy decisions on these issues.

III. THE COMMISSION'S PROPOSED POLICY AND RULE CHANGES GENERALLY ARE NOT JUSTIFIED

A. The Commission Has Not Demonstrated That A U.S. Settlements Deficit Requires The Proposed Policy and Rule Changes

1. The Commission's Own Policies Promote the Growth of the Deficit

As discussed above, and acknowledged by the FCC, certain of the FCC's own policies, particularly the approval of call back, refile and country direct services, tend to aggravate (or even cause) an imbalance in traffic flows. Such services offered by U.S. carriers result in increasing levels of U.S. outbound minutes for settlements purposes. These services have been growing rapidly in popularity, and the relative impact on U.S. outbound settlements has been growing as well.

While recognizing these effects, the FCC has long supported the offering of such services by U.S. carriers.[7] This has been true notwithstanding the vehement objection of many foreign telephone companies and administrations due to the deleterious effects that such services may have on the international revenues of a telephone company that experiences significant bypass due to call back. The Commission has reasoned that introduction of call back, country direct and refile creates positive incentives for foreign telephone companies to

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[7] See VIA USA Ltd. et al., 9 FCC Rcd 2288, 2290 (1994), on recon., 10 FCC Rcd 9540 (1995) (granting authorizations for international resale services including call back).

lower international collection rates to avoid such bypass. Thus, the Commission has affirmatively promoted services which tend to aggravate the imbalance of traffic between the U.S. and foreign countries.

The Commission essentially wants it both ways, authorizing, and indeed promoting, services which tend to aggravate the deficit and simultaneously complaining about the size of the deficit. To the extent that growth in the deficit results from the Commission's own policies, and not demonstrably from the policies and/or practices of foreign carriers and administrations, the drastic measures proposed by the Commission in this proceeding are unwarranted.

2. The Relevant Size Of Any U.S. Settlements Deficit Due to Above Cost Accounting Rates Has Not Been Demonstrated

Even if it made sense for the Commission to use the growth in a U.S. settlements deficit as an argument to set benchmark accounting rates, it has not properly calculated a relevant deficit. The Commission broadly estimates that "at least three-quarters of the $5 billion in outpayments is such a subsidy from U.S. consumers, carriers and their shareholders to foreign carriers."[8] Although the Commission does not explain the derivation o this estimate, it appears that the basis of it is a simplistic calculation of the difference between actual amounts paid and those that would have been paid using "cost based" accounting rates.

As mentioned above, much of the "deficit" reflects refile and reverse call services from which U.S. carriers earn substantial profits. U.S. carriers should be required to

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[8] It also does not distinguish that portion of the subsidy borne by U.S. carrier shareholders from that borne by U.S. consumers. Shareholder interests traditionally have not been protected by the Commission. As demonstrated earlier US consumers have not benefited from lower accounting rates.

provide specific information on actual and relative settlement minutes generated from such traffic, and such minutes should be deleted from any deficit calculation. Moreover, such calculations should be performed on a country by country basis. For example, as noted above, and acknowledged by the Commission, any "deficit" with Hong Kong is entirely due to call back, refile and country direct services. Thus, effectively there is no deficit with Hong Kong.

Also, the entire characterization of settlement outpayments as a "deficit" is misleading. Such outpayments cannot be considered a "deficit" without comparison with total revenues earned for call back and refile services provided through the U.S. In fact, U.S. carrier net international revenues have continued to increase, despite an increase in settlement outpayments. Clearly, despite settlement obligations to correspondents, U.S. carriers are still earning a healthy margin, and presumably are pricing their international services to maximize profits.

3. Any U.S. Settlements Deficit Has Not Been Shown To Be Caused By Above Cost Accounting Rates

As discussed above, no clear direct connection has been, or can be shown, between above cost accounting rates and settlements deficits. The real issue is not above cost accounting rates, but traffic imbalances that in turn are caused by various combinations of demographic factors, collection rate arbitrage within a given country and carrier arbitrage of relative settlement rates. Any of these factors, or their occurrence in combination may result in traffic imbalances that cause net settlement outpayments. The Commission has not demonstrated whether and/or how the singular effects of above cost accounting rates can be disentangled from these other factors. Thus, the Commission cannot show that U.S.

ratepayers suffer specific direct adverse impacts due to above cost accounting rates or that prescription of lower accounting rates would ameliorate the problem.

4. Any U.S. Settlements Deficit Has Not Been Shown To Cause Above Cost International Collection Rates

The Commission also asserts that the deficit itself causes above cost collection rates for U.S. consumers.[9] This, in fact was a major premise for the initiation of the Accounting Rates Proceeding.[10] However, as mentioned above, there is no direct or automatic relationship between reductions in accounting rates and corresponding decreases in U.S. international collection rates. The FCC has acknowledged that AT&T's international collection rates have not declined in proportion to accounting rate reductions that already have occurred.[11] As demonstrated, in the case of U.S. service to Hong Kong and 33 other countries, collection rates have risen.

B. No Adverse Impact On International Competition Has Been Demonstrated

1. Accounting Rates Have Not Been Shown To Cause Low IMTS Growth

The Commission asserts that calling patterns for IMTS are highly elastic and that reductions in accounting and settlement rates, which it claims would lead to lower collection charges, in turn would (i) "significantly stimulate traffic flows," increasing revenues for U.S.

[9] Notice at ¶ 18.

[10] Regulation of International Accounting Rates, Notice of Proposed Rulemaking, 5 FCC Rcd 4948, 4949 (1990).

[11] Regulation of International Accounting Rates, Notice of Proposed Rulemaking, 6 FCC Rcd 3434, 3435 (1991).